Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Federal-State Joint Board on	)	
Universal Service	)	WC Docket No. 05-337
	)	
Use of Auctions to Determine High-Cost	)	
Universal Service Support	)	

REPLY COMMENTS OF
THE SOUTH DAKOTA TELECOMMUNICATIONS ASSOCIATION, CAMERON COMMUNICATIONS, LLC, CLEAR LAKE INDEPENDENT TELEPHONE COMPANY, HANSON COMMUNICATIONS, INC., HARRISONVILLE TELEPHONE COMPANY, HILL COUNTRY TELEPHONE COOPERATIVE, INC., HINTON TELEPHONE COMPANY OF HINTON, OKLAHOMA, INC., SMART CITY TELECOM, SOUTH SLOPE COOPERATIVE TELEPHONE CO., INC., TOWNES TELECOMMUNICATIONS, INC., AND WIGGINS TELEPHONE ASSOCIATION

These Reply Comments are submitted by the referenced group of incumbent rural telephone companies, known as the "Rural USF Coalition", or "Coalition" who also filed initial comments in response to the Federal-State Joint Board's August 11, 2006 Public Notice on auctions. As noted in the Coalition's initial Comments, the constituent members are all recipients of high cost USF support, operate in high cost, low density areas, and represent a geographic reach which spans the western states to the east coast of the U.S. The Coalition's members represent, collectively, 46 rural incumbent carriers.

The reverse auction proposal constitutes an attempt by the Joint Board to address a problem of proliferating growth in the high cost fund. This concern is laudable, and many of the commenters address this sentiment. However, as many of the commenters note, including both those who represent public and private interests, reverse auctions promise to do more harm than good. The Rural USF Coalition's initial comments urge the Joint Board to focus on the root cause of growth in the fund itself, before considering reverse auctions as the primary considered solution. In this respect, the Coalition's comments discussed the FCC's recognition of competitive ETC ("CETC") designation as a source of the "dramatic" growth in the high cost fund. The Coalition further noted public financial reports that high cost amounts simply were flowing directly to the bottom line for such CETCs. Rural USF Coalition Comments, pp. 2-3.

Many commenters express similar, if not the same, views. The Joint Board should focus more specifically on why the high cost fund needs fixing before identifying solutions that address growth. The Coalition, and many others, demonstrate that once these root causes are identified, the solution is more directly identified and implemented.

These Reply Comments discuss the record thus far on this threshold issue on the growth of the fund. The practical and legal problems raised by reverse auctions, as identified by other commenters, also are discussed. The contrary views supporting reverse auctions, mainly relying on unsupported, doctrinaire economic theory, also are discussed.

<u>The Growth of the Fund</u>

The Coalition, and many others, have examined and discussed the root causes of high cost growth in the fund. The Comments cluster around a combination of rapid CETC designations, principally by the states, together with FCC programs that allow CETC per line compensation based on revenue streams wholly divorced from CETC costs.

For instance, CenturyTel, Inc. identifies a number of key recommendations to reduce pressure on the fund, including limiting the number of CETCs in a market (CenturyTel discusses one market having 10 ETCs, nine of whom are wireless), and requiring CETCs to actually invest in universal service projects. CenturyTel Comments, pp. 11-12. One of these recommendations also is to eliminate support from the ICLS and IAS program for CETCs. Id., at 12. CenturyTel points out that ICLS and IAS were created as access replacement mechanisms with the purpose of lowering ILEC access charges. CETCs have no such charges to lower, yet the associated revenues are available to them because they were included in the portable, high cost fund. CenturyTel notes NECA's calculation that approximately $600 million could be saved, annually, by removing this windfall from CETC high cost support. Id., p. 12 & n. 23.

The National Telephone Cooperative Association ("NTCA") likewise focuses on escalating CETC support as the root of the problem. Utilizing USAC filings with the FCC, it notes that CETC support has grown 870 percent between 2005-2006 – from $103 million to $1.03 billion. It further notes that, during the same time frame, ILEC high-cost USF support has remained unchanged at $3.17 billion. NTCA Comments, pp. 20-21 & n. 48. The National Exchange Carrier Association ("NECA") underscores this latter point based on GAO information, which reports that most of the perceived growth in the fund has come from shifting ILEC revenue requirements between access charges to universal service programs. NECA points out that the real growth in the fund is caused by payments to CETCs. NECA Comments, p. 6 & n. 19. The New Jersey Board of Public Utilities also agrees ("The number of supported networks is directly linked to the increase, particularly in the last several years.") New Jersey Board of Public Utilities Comments, p. 4.

In sum, as the Coalition argues in its initial Comments, the Joint Board should examine why the high cost fund is "broken" before it settles on reverse auctions as the fix. Coalition Comments, pp. 205. A number of commenters provide the data which demonstrates, clearly, that the growth of the fund lies at the feet of FCC and state policies, which have allowed CETC access to the fund, virtually unchecked. The remedy for this is not a reverse auction. Rather, the Joint Board should recommend an overhaul of the way CETC high cost support is determined, and of the way that CETCs are held to investment and maintenance responsibilities.

As discussed below, the initial comments demonstrate that additional problems plague the reverse auction proposal.

The Reverse Auction Proposal Is Not Practical

Many commenters have concluded that the practical problems associated with implementing auctions, and ensuring service in high cost areas in the aftermath, are severe. NASUCA, for instance, raises the critical public policy question as to what role quality of service or service capabilities should play, when the primary objective appears to be rewarding the low cost provider. NASUCA Comments, p. 7, no. 23. Likewise, NASUCA raises the very practical issue, key to a real-world analysis, as to what happens to service when the incumbent is the auction loser and transitions out of its carrier of last resort status. Id., pp. 8-9. NASUCA observes, accurately, that this transition issue is directly tied to the question of how much USF support would actually be reduced. Id. The net of NASUCA's analysis is plainly stated: "An auction mechanism would certainly be no simpler than the current mechanism with its mendable flaws." Id., p. 10.

Other state regulatory interests reject the proposal on similar grounds: "The reverse auction model does have the potential to lower USF assessment obligations. However, the Oklahoma Corporation Commission believes that there are far too many unanswered questions and potential unintended consumer consequences for reverse auctions to present a workable solution for controlling the size and growth of the high cost fund." Comments of The Oklahoma Corporation Commission, p. 9 (emphasis supplied. Accord, Comments of the Public Service Commission of the State of Missouri, pp. 2-7. ("Unfortunately, as explained in these comments, the MoPSC suggests the logistics of managing such a [reverse auction] fund are considerable. …the MoPSC strongly supports the Commission's efforts to stabilize and maintain the USF, but suggests a reverse auction process is not a reasonable solution.")

A number of rural companies who would be called upon to plan infrastructure deployment as auction winners, or to exit as an ETC as auction losers, also question the workability of the proposal. CenturyTel points out the daunting administrative problems that attend choosing a "winner" where price and service quality cannot be easily compared by the auction administrator. CenturyTel Comments, p. 17. These same comments discuss similarly difficult problems in enforcing performance of a winning bid, particularly where only the ILECs are regulated meaningfully as to service quality and rates, today. Id., pp. 18-19. CenturyTel accurately observes that consumers will bear the ultimate price for the failure to perform by an auction winner. Id.

NTCA, representing well over 500 rural ILECs, observes, as does CenturyTel, that it is consumers who are at the greatest risk with this experimental program. NTCA Comments, p. 13. NTCA devotes several pages of discussion to the issue of post-auction enforcement to ensure compliance with universal service funding objectives, and to the issue of stranded investment and legal confiscation issues where incumbent carriers are no longer recipients of high cost funding. Id. pp. 12-15.

The bottom line is that there is an overwhelming likelihood that reverse auctions are unworkable. And, although there may be a set of solutions to make it workable, they are impractical, given the "mendable" problems, as NASUCA puts it, of the current mechanism.

The Reverse Auction Proposes a Sweeping
Elimination of the Rate of Return Paradigm

The Coalition discussed the obstacle which the Supreme Court's decision in Smith v. Illinois Bell Telephone Co., 282 U.S. 133, 75 2. Ed. 255, 51 S.Ct. 65 (1930) presents to the auction proposal. Coalition Comments, pp. 5-7. In short, the Smith Court long ago recognized that interstate operations impose costs upon commonly used telephone plant. In the ensuing 75 years, such plant costs, mainly non-traffic sensitive in nature, became the subject of high cost funding. The Courts have had occasion to address these costs, and have found them not to be a subsidy. See e.g., Coalition Comments, p. 7. Such legitimate, interstate costs are now, because of federal policies, hardly borne at all through interstate access charges. Rather, they have increasingly been shifted into the portable, high cost fund. See NECA Comments, p. 6 & n. 19.

The implementation of an auction mechanism introduces the near certainty that incumbent LECs, now subject to the FCC's Title II regulatory authority, will face systemic revenue requirement shortfalls. Such will occur whether an incumbent LEC either is an auction loser, or a winner forced to bid down to confiscatory levels. NECA cogently explains how the auction mechanism would fundamentally change and, perhaps, destroy the existing rate of return mechanism. NECA Comments, p. 11. Simply put, there is an overwhelming likelihood that shortfalls will occur, and there is no mechanism to offset them. The Coalition submits that incumbent LEC investment has Constitutional and statutory protections which are implicated by the reverse auction scheme. At the very least, the evisceration of the rate of return model is so directly tied to the proposal that it would represent a radical FCC policy departure. This cannot be lawfully accomplished absent a more searching, intensive agency inquiry than the instant Joint Board Public Notice.

Indeed, even auction supporters, like AT&T, recognize the tie between carrier of last resort obligations and the auction construct. Comments of AT&T, Inc., p. 11. The Joint Board should not recommend high cost auctions to the FCC within this context. It can only be implemented, as presently contemplated, at the expense of goring the rate of return mechanism. Such a change is certainly a radical departure from the social contract that has underpinned universal service for decades. The Joint Board accordingly is urged to consider more targeted and calibrated alternatives to accomplish the needed reform of the high cost mechanism.

The Coalition Supports Targeted Alternatives

The Coalition supports the proposals submitted by NTCA in its comments as a way to accomplish the goals of the reverse auction proposal, with much less risk to consumers and those providers who rely on universal service support for the provision of affordable communications services. Specifically, the Coalition supports the elimination of the identical support rule; the application of a meaningful public interest test for future ETC designations; and the expansion of USF contributors to include all broadband service providers. The Coalition urges the Joint Board to focus on these reforms rather than the reverse auction proposal.

Conclusion

Based on the foregoing, the Coalition urges the Joint Board to adopt the recommendations contained herein and in the Coalition's comments filed in this proceeding.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the forego Reply Comments was served this 8th day of November, 2006, by electronic filing and U.S. mail to the persons listed below.

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